1946

THE SENATE OF CANADA

PROCEEDINGS

OF THE

STANDING COMMITTEE ON BANKING AND COMMERCE

to whom was referred the Bill A-5, intituled:
"An Act respecting Bankruptcy."

No. 6

WEDNESDAY, JULY 31, 1946

CHAIRMAN

The Honourable Elie Beauregard, K.C.

WITNESSES:

Mr. W. J. Reilley, K.C., Superintendent of Bankruptcy.

Mr. A. W. Rogers, K.C., Montreal, P.Q., Secretary, The Canadian Bankers' Association.

APPENDIX:

Brief filed by Mr. A. W. Rogers, K.C.

OTTAWA
EDMOND CLOUTIER, C.M.G., B.A., L.Ph.,
PRINTER TO THE KING'S MOST EXCELLENT MAJESTY
CONTROLLER OF STATIONERY
1946

ORDER OF REFERENCE

EXTRACT from the Minutes of Proceedings of the Senate for 13th May, 1946.

Pursuant to the Order of the Day, the Honourable Senator Robertson moved that the Bill (A-5), intituled: "An Act respecting Bankruptcy", be now read a second time.

After debate, and—

The question being put on the said motion.

It was resolved in the affirmative.

Ordered, That the said Bill be referred to the Standing Committee on Banking and Commerce.

L. C. MOYER,
Clerk of the Senate.

STANDING COMMITTEE ON BANKING AND COMMERCE

The Honourable ELIE BEAUREGARD, K.C., *Chairman*

The Honourable Senators

Aseltine	Euler	Marcotte
Aylesworth, Sir Allen	Fallis	McGuire
Ballantyne	Farris	Michener
Beaubien (*Montarville*)	Foster	Molloy
Beauregard	Gershaw	Moraud
Buchanan	Gouin	Murdock
Burchill	Haig	Nicol
Campbell	Hardy	Paterson
Copp	Hayden	Quinn
Crerar	Howard	Raymond
Daigle	Hugessen	Riley
David	Jones	Robertson
Dessureault	Kinley	Sinclair
Donnelly	Lambert	White
Duff	Leger	Wilson—(47).
DuTremblay	Macdonald (*Cardigan*)	

MINUTES OF PROCEEDINGS

WEDNESDAY, July 31, 1946.

Pursuant to adjournment and notice the Standing Committee on Banking and Commerce met this day at 10.30 a.m.

Present:

The Honourable Senators: Beauregard, Chairman; Asseltine, Burchill, Gershaw, Gouin, Haig, Hardy, Howard, Hugessen, Jones, Kinley, Leger, Macdonald *(Cardigan)*, McGuire, Moraud, Robertson, Sinclair, White.—18.

In attendance: Mr. J. F. MacNeil, Law Clerk and Parliamentary Counsel of the Senate.

Bill A-5, An Act respecting Bankruptcy, was further considered.

Mr. W. J. Reilley, K.C., Supt. of Bankruptcy, was again heard.

Mr. A. W. Rogers, K.C., Montreal, P.Q., Secretary, The Canadian Bankers' Association, submitted a brief and was heard.

Further consideration of the Bill was postponed.

Attest.

R. LAROSE,
Clerk of the Committee.

69415—1½

MINUTES OF EVIDENCE

THE SENATE

OTTAWA, Wednesday, July 31, 1946.

The Standing Committee on Banking and Commerce to whom was referred Bill A5, an Act respecting bankruptcy, met this day at 10.30 a.m.

Hon. Mr. BEAUREGARD in the chair.

The CHAIRMAN: Gentlemen, we are to hear from Mr. A. W. Rogers, K.C., Secretary of the Canadian Bankers' Association.

Mr. ROGERS: Mr. Chairman and honourable senators, we realize that it is very difficult for any one drafting legislation designed to remedy certain evils to cover the ground adequately without perhaps going a little too far one way or the other. The study being made by your Committee, and the opportunity afforded various interests and organizations to present what, we hope, are constructive criticisms, will, I think, help materially in making the legislation more effective. My own experience years ago in drafting legislation impressed on me that sometimes there is a tendency for the draftsman in trying to remedy an evil to cut too wide a pathway and so get into territory that he would rather not have touched. It is only when an opportunity like this is afforded to discuss the matter generally with the public before a tribunal such as yours that the pertinent points can be brought out. Any submissions we may make are intended to be not merely critical but, we hope, constructive, and we trust they will have some beneficial effect.

There are some points arising from interpretation which I think can better be dealt with in connection with some of the sections, but there is one particular definition I might mention, that of "creditor" in section 2 (o). This definition has now been amended to include a secured as well as unsecured creditor. No doubt the definition in general terms of a creditor would have sufficed, but when you specifically mention that it is to include secured creditors, it has certain effects, as will appear from consideration of certain sections of the Bill that are related to the definition. For instance, in section 19, subsection 1:—

> A composition accepted by the creditors and approved by the court shall be binding on all creditors with claims provable under this Act, but shall not release the debtor from the debts and liabilities referred to in section one hundred and fifty-four of this Act except to such an extent and under such conditions as the court expressly orders in respect of such liability.

By that broad phraseology the composition would be binding on all creditors, including secured creditors, by reason of the specific definition; whereas, it was probably the intention that it would be binding only upon the creditors who had not had an opportunity of obtaining securities for their debts.

In section 26 the same question arises with respect to a stay of proceedings. The first subsection provides generally that during the bankruptcy of a person or on the filing of a proposal of composition no creditor shall have any remedy against the person who is to be put into bankruptcy "or shall commence or continue any action, execution or other proceedings for the recovery of a debt provable in bankruptcy," unless with leave of the court. As the provision stands in the Act, subsection 2 went on to deal with the position of secured creditors and it stated that, "subject to the provisions of certain other sections, any secured creditor may realize or otherwise deal with his security as if this section had not been passed, unless the court otherwise orders." This of course is quite a proper proceeding, for it the court felt a secured creditor should not realize his security, it might on special representations make an order requiring the secured creditor not to realize.

Hon. Mr. LEGER: The only change would be the necessity of applying to the court: that is the only effect, is it not?

Mr. ROGERS: The change would be to overcome the effect of subsection 2 of the Act and require a secured creditor to get leave in every case before realizing his security. That is because of the new definition of creditor and the addition to subsection 2 of the words "and the preceding subsection." This completely nullifies the intention of subsection 2, which was to remove the secured creditor from the restrictions of subsection 1.

Hon. Mr. HUGESSEN: Your objection is to the words "and the preceding subsection"?

Mr. ROGERS: Yes. The effect is brought about by those words and also by "creditor" as now defined. The new definition of the word includes a secured creditor. So the original provision whereby a secured creditor was given certain freedom of action is offset and really nullified.

Hon. Mr. MORAUD: What was the definition before?

Mr. ROGERS: It is in the bill on the right hand side.

Hon. Mr. MORAUD: Oh, yes.

Mr. ROGERS: It was not a general definition, it was specific with relation to particular cases. But the effect of the specific amendment is perhaps dangerous, having regard to the effect of its inclusion in the Act in that way.

Hon. Mr. MORAUD: The former definition was too long, and this one is too short.

Mr. ROGERS: Then there is another point in the definition of the word "transaction". It is so general that it would be very difficult to imagine anything that would not come within the transaction. While it is quite true that it is necessary to define some words in order to prevent a lot of repetition, particularly in section 68 and others, the new definition seems to cover so wide a field that it goes beyond what is now in the Act.

Hon. Mr. LEGER: Would it be necessary to define it at all?

Mr. ROGERS: I think the court would define transaction as being a business dealing of some sort.

Hon. Mr. MORAUD: "Transaction" in our civil code has not the same meaning at all as "transaction" in this bill.

Mr. ROGERS: It is so difficult to say what might be meant by "anything done or left undone by a person which affects another person's rights and obligations out of which a course of action may arise". It is so broad that it is rather difficult to say what its effect might be. Section 64 of the Act commences,

> Every conveyance or transfer of property or charge thereon made, every payment made, every obligation incurred and every judicial proceeding taken or suffered . . .

It was in that sense fairly precise and rather limited, but the definition in this bill is very broad, and it is difficult to know just how far its effects may go. Perhaps when we come to one or two of the other sections its effects will be a little more apparent.

Section 3 covers acts of bankruptcy. The inclusion of a new act of bankruptcy in paragraph (*d*) of this section goes somewhat further than the preceding paragraph (*c*), which deals with something of that nature. It reads:—

> If in Canada or elsewhere he makes any conveyance or transfer of his property or any part thereof, or creates any charge thereon, which would under this Act be void as a fraudulent preference if he were adjudged bankrupt.

No one could quarrel with that.

Paragraph (*d*) covers:—

> Any conveyance or transfer of his property or any part thereof, or creates any charge thereon, which would have the effect of defrauding, delaying or defeating his creditors or any of them.

Hon. Mr. LEGER: In other words, he could not mortgage his property.

Mr. ROGERS: It is just a question whether under certain circumstances a mortgage which might be taken and given in all good faith would come within this, because undoubtedly it would have the effect of delaying or defeating his creditors or any of them. That is, one creditor might be defeated by the giving of a certain security; there might be no fraud intended, yet it would be an act of bankruptcy. Our feeling is that it goes further than should be necessary.

I turn now to page 6. Paragraph (i) of section 3 relates to bulk sales. Under the paragraph in the Act a bulk sale made without complying with the requirements of the provincial laws would be an act of bankruptcy. But the phraseology now is such that the whole purpose of the paragraph is changed, and if anyone makes a bulk sale "wherein the sale price will not be sufficient to pay his creditors in full" that sale constitutes an act of bankruptcy. The danger is that a man might make a bulk sale and the proceeds would be insufficient to pay his creditors in full, but he might have other assets, including bank deposits, from which the balance of his creditors' claims could be paid, but the definition could result in his being forced into bankruptcy regardless of his real financial position.

Hon. Mr. LEGER: That would come in conflict with our provincial Bulk Sales Act.

Mr. ROGERS: Perhaps it calls for a sale under the provincial law, but it states that an act of bankruptcy will have been committed if the sale price is not sufficient to pay all creditors in full. It ignores the fact that there might be other assets, so the sale would be perfectly sound and the man absolutely solvent. Perhaps the amended paragraph is cutting too wide a swath from that point of view.

In paragraph (i) of section 3 we find another point of difficulty. It is an act of bankruptcy if the man "ceases to meet his liabilities generally as they become due." That, of course, has always been in the Act. But the paragraph is amended to read:—

> . . . . .or fails to pay any particular debt or debts after repeated demands for payment.

If it is going to constitute an act of bankruptcy when a man fails to pay any debt after repeated demands for payment, it would constitute a very serious encroachment on the right of an individual to contest claims of debt on sound legal grounds. While there may have been some cases of uncertainty, as Mr. Reilley states, it seems to me that where a man might be stalling and too much delay might result in the loss of some assets, it is just a question whether legislation should go so far as to make it difficult for others to do business with a man, and certainly this amendment would expose the individual to threats of bankruptcy proceedings at the hands of an unscrupulous creditor unwilling to establish his claim to the debt in the civil courts. It seems to us to be going too far.

There is a small point in section 18, subsection 11 on page 18 of the Bill, which we wish to make.

The subsection provides:—

> On the filing of a proposal the property of a person not bankrupt shall be deemed to be under the custody of the court until the proposal is finally disposed of by the court and any alienation thereof except in the normal course of business shall be null and void.

We think this probably means any alienation by the debtor. But actually there might be property of the debtor on which he has given a valid security in such a way that the person who holds that security is entitled to realize on it, and normally make good title. This new subsection would throw a cloud on that title if it is going to cover alienation by anybody of the property of the debtor. We think it would be better to clarify the wording by stating "any alienation by the debtor." This is no doubt the intention of the subsection.

In section 39, subsections 11, 12, and 13, there is a small point on administration. It is quite proper that the Superintendent should have access to the bank accounts or any other information he might want. The difficulty is that banks, by reason of the contract between depositor and banker, are under an obligation of secrecy. That obligation is so strong that if a bank discloses its customer's affairs it is liable in law. So the banks before giving information would want to be sure that they were giving it to properly authorized persons. The Superintendent could not do all the work himself, and presumably he may retain accountants to do it on his behalf. We suggest therefore that the Superintendent have power to authorize a person to act on his behalf. Then if that authorized person comes to a bank to secure information the bank would be protected. That is the usual procedure under the Income War Tax Act and a number of other statutes, both Dominion and provincial, where it is necessary to have access to bank accounts.

Hon. Mr. MORAUD: Don't you think, Mr. Rogers, that that again is an invasion by an officer of the department, of the jurisdiction of our courts? If an investigation is to be made, it should be made under the direction of our courts.

Mr. ROGERS: It is certainly more desirable. But we have had to submit with the best grace possible to similar provisions in Dominion as well as provincial legislation, where an officer is clothed with certain powers, as under the Securities Act and the Income War Tax Act and the Excise Act, and can examine bank accounts. It certainly would be more desirable if all this could be done under the aegis of the courts, as the honourable senator suggests, but in view of what has already happened we could scarcely urge that. All we can ask is that there be a clear-cut delegation of authority. If that is to be the case, we shall have to submit with good grace.

Hon. Mr. MORAUD: I submit that this should be done under the direction or authority of a court of justice.

Mr. ROGERS: There is something of that, sir, in subsection 12:—

> The Superintendent or anyone in his behalf may with the leave of the court examine the private books, records and documents and bank accounts of a trustee. . . .

That brings in the principle there.

Hon. Mr. MORAUD: There is nothing of the kind in subsection 11.

Mr. ROGERS: No, there is nothing of that nature in subsection 11. It goes your way in subsection 12. But it is just as you honourable senators wish in matters of that sort. As I say, we have to submit with grace, as many others have, to requirements of that nature where investigations are conducted by representatives of the Crown without the authority of the court, but under the authority of a statute. We always insist on absolute compliance with the requirements of the order of the court or the statute, because otherwise we would be liable, and financially we cannot afford to accept that liability.

Sections 68 and 69 have given rise to a considerable amount of doubt as to their effect on banking transactions as well as others. Section 68 will be found on page 54 of the Bill. Subsection 1 provides:

> Every transaction—

which, as you have seen, is very broadly defined now.

—whether or not entered into voluntarily or under pressure by an insolvent person becoming bankrupt within three months thereafter resulting in any person or any creditor or any person in trust for such creditor or any surety or guarantor for the debt due to such creditor obtaining a preference advantage or benefit over the creditors or any of them shall be deemed fraudulent and void as against the trustee.

The danger of that broad provision, it seems to us, is that the question of intent is no longer an element. It is still a pretty general requirement in almost all criminal offences that intent is an element of the deed and, in many cases, a man is entitled to bring in evidence that his intent was honest or proper, and the intent may vary considerably the gravity of the crime. Yet here the effect alone is to be the arbiter of the situation. If there is any "advantage or benefit over the creditors or any of them"—which means any one of them—the transaction is deemed to be a preference, and the person that took part in it is tainted with fraud. That is almost as bad as being tainted with criminality, because no one wants to be put in a position of that sort. A man may have entered into a transaction in perfectly good faith and it may have resulted in advantage to him over some single creditor, yet the transaction would be fraudulent.

Hon. Mr. LEGER: What about its effect on a bank advancing money on a bill of lading?

Mr. ROGERS: That is precisely what I was coming to, sir. Banks do business in various ways with different customers. A bank frequently does business on bills receivable, with a promise by the customer to give security if the bank requires it. A situation may develop, due either to general business conditions or a change in the individual's situation, which from its experience indicates to the bank that it probably had better get security, and this it will ask for and obtain. Undoubtedly in cases of that sort there is some benefit to the bank as against other creditors or as against a single creditor. The onus now would be upon the bank to prove the transaction was a proper one. By reason of the phraseology of section 69 as now amended the onus is a very difficult one to satisfy, because it has to be shown that the transaction is for adequate and valuable consideration and without reason to suspect any insolvency. Yet by reason of the broad definition of bankruptcy it might well be—I realize this is stretching the point—that as bankruptcy would be constituted under the bill, failure to pay a particular debt, if the bank knew that it could hardly be said that it did not have some reason to suspect insolvency. You do not know how far the courts may go in that event. While it is an extreme illustration, there might be other cases where the bank could not come in and satisfy the onus, yet under the Bank Act there is a provision for banks taking additional security. For instance, a bank is not allowed to lend money on mortgage of land, but it is allowed to take such a mortgage as additional security; that is, if additional security is necessary to protect not only the bank but the depositors, because that is the important part of it, and that is why parliament has authorized those provisions. If a bank is going to be exposed to having it established that the taking of that security was a preference, it might invalidate the security and the bank might refrain from putting itself in that position. As a result the banks' security would be weakened and the credit standing of people doing business with banks would be affected. To offset this banks would have to take more security at the outset than perhaps is taken at the present time. The combined effect it seems to us is rather serious and could go a long way towards making ordinary business rather difficult.

If you look at subsection 2 of section 68 you will find it designed to enable the trustee to invoke provincial laws in order to invalidate certain transactions.

No one can have any quarrel with that, but the phraseology is so broad—it certainly was not so intended I believe—that the trustee could avail himself of any law in any province of Canada regardless of the locality of the debtor or of the property affected. There might be some extreme statute in British Columbia and the bankruptcy might have taken place in Quebec, yet as this subsection is worded the British Columbia law might be invoked in relation to the bankruptcy in Quebec, although the debtor did not reside in British Columbia nor had he any assets there. It seems to us this subsection should be redrafted to make it clear that that is not intended. As you gentlemen are aware, before the enactment of the Bankruptcy Act the provinces had certain legislation in the field of bankruptcy, such as the assignments and preferences acts. When the bankruptcy statute was enacted it was universally felt, and probably held, that the Bankruptcy Act would suspend the operation of the provincial laws. A question would now arise whether this amendment would remove that suspension. That is one of the difficulties which arises from the use of the more general phraseology such as appears here.

Before leaving subsection 1 of section 68, I may say that over all the years there have been many decisions on the effect of the provision that there should be intent established before a transaction is declared void for fraud. Those decisions will pretty well have to be abandoned under the proposed amendments, and that might be unfortunate in a number of different ways. But taking it from the point of view of bank transactions, it has been held that it would not be a preference for a bank to transfer a credit from one account of a customer to another account which was in debt. It is still a question whether under this broad phraseology that would be permitted. It would have to come before the courts again until it was declared authoritatively whether a bank could exercise its privilege of consolidating accounts, which it has always hitherto been allowed to do.

Then there are other cases where they might have difficulty. It has been held that payments in the ordinary course of business would not be regarded as constituting a preference. It might be a question whether payment on a debt which was matured and due the bank would be contrary to these provisions. In another case it has been held that payment of secured creditors should not be within the provision as it stands now in the Act. That question would have to be settled in the courts and until that had been done in an authoritative manner, the banks would not know how far to go in their ordinary day-to-day dealings with their customers. It seems to us that this amendment goes much further than may be necessary and will make it very difficult for people doing business.

In subsection 3 of section 68 there is reference to a secret transaction between the bankrupt and "any other person". It is difficult to know just what that might cover. As I have explained, there is an implied secrecy between banker and customer. Under this amendment that would be a secret transaction and might give rise to difficulties because it comes within that definition.

Subsection 5 of section 68 has already been referred to in a sense, but it does make it clear that evidence of intent on the part of either party to the transaction shall not be available as a defence to support such transaction if in fact a preference, benefit or advantage was obtained over the creditors or any of them. That is a pretty broad provision. A man would not be able to come into court and show good faith if in fact a preference, benefit or advantage was obtained. The transaction would be regarded as fraudulent and would be voided. In the Bankruptcy Act of 1910, as you gentlemen will remember, there was a provision of that sort, but in 1920 those words were transferred to subsection 2 and formed part of a prima facie presumption, which of course was susceptible of rebuttal. In other words, it might be a presumption of law from certain facts that the transaction was a benefit and improper, but evidence could be adduced to show that such was not the case. This new provision will

change that, and if any advantage or benefit or preference was obtained over any creditor the transaction will be invalidated. The effect of that would certainly be serious on ordinary business procedure.

I have a few more observations to offer with regard to section 69. As this section now stands in the Act, in order to enable a man to establish that he did not obtain a preference he must prove that the transaction was entered into in good faith before the date of the receiving order and without notice of any available act of bankruptcy. The new provision would add the following requirements: That the valuable consideration be adequate, that there be no knowledge of the insolvency or commission of an act of bankruptcy, that there be no reason to suspect insolvency or commission of an act of bankruptcy. This would really give rise to difficulties in a bank transaction. For instance, it would be very difficult in the case of a security given, particularly an additional security, where a bank felt positively that it was given for adequate and valuable consideration when it was really given for money already loaned and upon which some security had been taken, but that security perhaps had lost value in some way and the situation had developed to a point where the bank felt some additional security of real estate or something of that sort was necessary. The shifting of the onus here, which would require the bank or other person to bring itself within the protection of section 69 (1), is going to be much more difficult to comply with by reason of that and also because of the very broad definition of insolvency, "reason to suspect insolvency or commission of an act of bankruptcy." We have discussed that and have seen that the failure to pay one particular debt after repeated demands is an act of bankruptcy. As a result a bank, knowing the man's failure to pay the debt was for a perfectly good reason, might be regarded as having knowledge that he had committed an available act of bankruptcy, and therefore could not bring himself within the protection, and the transaction would be invalid. There are so many uncertainties arising from the proposed provisions that our feeling—which I think is common with that of other members of the commercial community—is that it would be better to adhere to the existing provisions and the body of law built up under them, over a period of twenty-five years, than cut loose from them altogether and throw the whole situation in the air so that no one would know just where he stood.

I should like now to make a rather broad jump to section 110 at page 72 of the Bill. It deals with proof of claims. Subsection 1 reads:—

> Every creditor shall prove his debt as soon as may be after the filing of a proposal for a composition or after the bankruptcy—

Then there is this penalty added:—

> —otherwise he shall not be entitled to share in any distribution that may be made.

It is quite proper to impose a penalty if a man does not prove his debt, but how soon is, "as soon as may be"? It seems to me there ought to be some precise method of ascertaining when a debt should be proved within some time limit. One court might hold a month was the time; another, that two years was not out of the way. Without some clear-cut definition it is very difficult to know where you are.

Hon. Mr. Haig: What would you suggest, six months, one month?

Mr. Rogers: I really would not make a sound suggestion because I think it could come better from the Superintendent of Bankruptcy himself, who has had wide experience in bankruptcy.

The Chairman: That is just a suggestion you are making?

Mr. Rogers: Yes. He suggests "as soon as may be." But I think when he appreciates the difficulty of imposing a penalty for failing to prove a debt within a definite time, he will realize that it would be wise to set a time limit. There are other time limits in the Act, six months, three months and so forth, but I should think a fair time limit could be set. I really have not had enough practical experience of bankruptcy matters to make a sound suggestion. So I would rather leave it to those who have greater knowledge, and wider experience. I am sorry, but I am afraid that is as far as I can go.

Now, section 124. As the explanatory note indicates, this is new and purports to do away with the law of set-off, which is said to differ in important respects in the several provinces. It is difficult to know just what is meant by "mutual dealings." The banks have the right of set-off, that is, the right of setting-off one debt against another, or one debt against a credit, and that sort of thing. Whether this section is intended to prevent that being done we do not know, but we feel that it might be looked at with more care to see what the effect might be. It might go further than was intended. We should not think that the ordinary rights of setting one account off against another would be intended to be interfered with, but the language and the explanation would indicate that the law of set-off is not to be observed except in accordance with section 124.

There is a little point in section 125, subsection 7:—

> The trustee shall not be liable for the costs of a creditor proving any claim if in the opinion of the court the trustee acted in good faith or was justified in requiring the claim to be proved before the court otherwise the costs of proving a claim shall be in the discretion of the court.

Our feeling is that if the trustee be given carte blanche he might go the length of contesting every claim and putting everybody to the proof, and the way the onus provisions have been changed it is going to be very difficult to sustain the validity of any transaction. The result would be the trustee would not be liable for any costs, and the effect might not be good. It seems to us that there ought to be something which would leave the trustee clearly in the hands of the court, and the court's discretion should govern the question of costs in all cases; otherwise the effect might be too sweeping. True, he is not going to be liable if the court feels he acted in good faith and was justified. We submit that the question of liability for costs should be left entirely in the discretion of the court, particularly if the onus is shifted as proposed in section 69 (2).

Section 126 deals with scheme of distribution. Subsection 1 provides:—

> Subject to the rights of contractual secured creditors the proceeds realized from the property of a bankrupt shall be applied in priority of payments as follows:—

It is realized of course that there has been a great deal of difficulty in establishing priority of claims, and there ought to be some such section as this, but the difficulty is the use of the words "contractual secured creditors" ignores certain statutory situations. For instance, under the Bank Act a bank is given a statutory lien on the shares of its shareholders. That certainly is not contractual and would not be covered by this section. Then there is a banker's lien at common law on the property of a debtor which may be in the bank's hands, such as securities, which perhaps may not have been hypothecated, but the bank has certain rights there just as the solicitor has at common law. Neither of these is contractual. It seems to us that the word "contractual" should go out. To make it doubly clear probably there should be a clarification with regard to the proceeds realized by the trustee. Certainly it is not intended, we think, to cover proceeds realized by secured creditors, because naturally those proceeds go to meet their claims, although of course if there is any surplus that must be paid

over to the trustee to be held in trust by him. It seems to us that as worded there it leaves the matter open to doubt, that the section covers all proceeds realized whether by secured creditors or otherwise.

Hon. Mr. HAIG: Would you say therefore that a debtor who had left papers with his solicitor, on which the solicitor had done a certain amount of work and had at common law a lien on them, would come under that provision?

Mr. ROGERS: The subsection reads:—

> Subject to the rights of contractual secured creditors the proceeds realized from the property of the bankrupt shall be applied in priority of payment.

You would not be a contractual secured creditor.

Hon. Mr. HAIG: I promise to look closely into that section.

Mr. ROGERS: I think it was not intended to go that far, but it has that effect.

Hon. Mr. HAIG: As far as I am concerned, I promise to see that it does not go that far. That is the only security we lawyers have.

Hon. Mr. MORAUD: In our province we have two sections in the code under which certain creditors are not contractual.

Hon. Mr. HAIG: We have woodsmen's liens and other liens of that nature in our province.

Mr. ROGERS: Yes, there are many common-law liens.

Hon. Mr. HAIG: In Manitoba we may have gone too far in giving liens to workmen under certain conditions. For instance, we have given liens on wood in the bush, and all that kind of thing.

Hon. Mr. LEGER: We have done the same in New Brunswick.

Mr. ROGERS: Their name is legion throughout the west particularly, and they would have to be considered.

I wish to thank you, gentlemen, for the privilege of making these representations. I have tried not to be carpingly critical, but rather to make constructive suggestions. We realize the difficulty faced by the draftsman and his great ability and wide range of knowledge with respect to the law of bankruptcy. We feel that after sifting the representations we have made and the suggestions you have received from other quarters it will be possible to develop a better Bankruptcy Act than the present one. Certainly no one would wish otherwise.

APPENDIX

BRIEF FILED BY MR. ROGERS, SECRETARY OF THE CANADIAN BANKERS' ASSOCIATION

The Honourable Elie Beauregard, Chairman,
and Members, of the Senate Standing Committee
on Banking and Commerce:

Senate Bill A-5—An Act Respecting Bankruptcy

In the presentation of these observations concerning the above Bill, on behalf of the chartered banks of Canada, it is not intended to deal with the provisions of the Bill as they affect the public generally. Representations along particular lines have already been made to your Committee by various organizations so it is felt that we would be more helpful to the Committee and to the law officers of the Crown responsible for the drafting of the Bill if these comments and suggestions were confined as far as possible to the provisions of the Bill as they appear to affect the chartered banks in their ordinary course of business.

Interpretation

There are a number of provisions in the interpretation section of the Bill which, viewed in the light of their use in subsequent specific sections, give rise to objections which will be discussed in more detail under such sections. Brief reference only will therefore be given to certain paragraphs of the interpretation section.

Section 2 (*b*)—"adequate valuable consideration"

While the definition corresponds quite closely to that of the present 65(2), its operation under the proposed shifting of the onus of proof in the proposed section 69(2) might be serious, as will be explained later.

Section 2(*o*)—"creditor"

This definition goes beyond the present one to include a secured creditor although the latter term is separately defined in 2(*ee*). The inclusion of secured creditor in the definition of creditor would be confusing as will be apparent in the consideration of subsequent provisions.

Section 2(*jj*)—"transactions"

It is appreciated that this new definition has been inserted in order to remove certain detailed phraseology from the present section 64 which commences "Every conveyance or transfer of property or charge thereon made, every payment made, every obligation incurred and every judicial proceeding taken or suffered . . ." A comparison of these words with the new definition indicates that "transaction" defined as proposed goes much further than the present provision and covers not only positive acts but includes instances of inaction, and even omission. It is difficult to anticipate the effects of so broad a definition. It would seem advisable to have a tighter definition at the outset, more in keeping with the provisions of the present statute.

PART I

Acts of Bankruptcy

Section 3(*d*)—"other conveyance or transfer"

This includes any conveyance or transfer of property or charge thereon, which would have the effect of defrauding, delaying or defeating any creditor, and goes considerably further than (*c*), which would only include such transactions if they would be void under the Act as fraudulent preferences if a debtor

were adjudged bankrupt. The new provision would include the giving of any security to a bank under section 88 of The Bank Act or by way of additional security. The giving of such security could be treated as an act of bankruptcy if any creditor other than the bank asserted that it would delay or defeat him in his efforts to collect an alleged debt. It would be opening the door very wide if a man giving security to his bank in the usual course of business could be thrown into bankruptcy by a creditor although the transaction was an ordinary banking one which took place in complete good faith on both sides. Banks make advances to customers frequently and take only a promise to give security on goods to be purchased with the money and a promise to give additional security if required. The giving of either type of security for which provision is made in the Bank Act should not constitute an act of bankruptcy. Again, a bank, noticing changes in general market developments or in the customer's business, might deem it advisable to obtain more specific security as an added safeguard. The taking of additional security in such cases should not expose the customer to bankruptcy proceedings. The effect of so broad a change would tend to make it more difficult for certain types of businessmen to obtain credit.

Section 3(i)—"bulk sale"

This would be an act of bankruptcy differing altogether from the corresponding present one, which constituted the making of a bulk sale without complying with the relative provincial Bulk Sales Statute. The new provision would make any bulk sale under provincial legislation an act of bankruptcy if the sale price proved insufficient to pay all creditors in full, and in view of the broad definition of "creditor" already referred to this would include secured as well as unsecured creditors. The definition ignores the possibility that the bulk seller may have outside assets, including bank deposits, from which the balance of his creditors' claims could be paid, but the definition could result in a man being forced into bankruptcy regardless of his real financial position.

Section 3 (1)—"ceasing to meet liabilities"

The enlargement of this definition from "ceasing to meet liabilities generally as they become due" to the inclusion of failure to pay any particular debt after repeated demands for payment, would constitute a very serious encroachment on the right of an individual to contest claims of debt on sound legal grounds. It would expose him to threats of bankruptcy proceedings at the hands of an unscrupulous creditor unwilling to establish his claim to the debt in the civil courts. The banks would not like to have their customers subjected to unjustifiable bankruptcy proceedings for the collection of such a debt.

PART II

Composition, Extension or Scheme of Arrangement

Section 18(11)—"pending disposition of proposal, property of debtor under custody of court"

As this new subsection stands it would be too broad for it purports to nullify any alienation of a non-bankrupt person's property pending the disposition of the proposal. As worded it is wide enough to cover any disposition of property by a creditor such as a bank which has been given security thereon. While the exception of an alienation in the ordinary course of business might suffice it would probably be better to clarify the wording by stating "any alienation by the debtor", to cary out the true intention of the provision.

Section 19(1)—"approval binding on creditors but does not release debtor from liabilities mentioned in section 154"

In view of the definition of "creditor" to include secured creditors, in section 2(*o*), and the broad phraseology "shall be binding on all the creditors with

claims provable under this Act", this provision would be too broad in its effect. Restriction of the definition of "creditor" to exclude unsecured creditors would cure this difficulty.

PART III

General

Section 26(1)—"stay of proceedings"

Here again the definition of "creditor" in section 2(*o*) to include a secured creditor would make impossible for the latter without leave of the court to realize upon his security or avail himself of any remedy in respect of the property covered thereby. This would be contrary to all previous practice and would constitute a complete reversal of the settled law that property of the bankrupt covered by security given to a secured creditor need not be affected by the bankruptcy.

Section 26(2)—"secured creditors"

As the corresponding provision stands in the present Act, it is intended to authorize the secured creditor to realize upon his security "unless the court otherwise orders". The effect, however, of making this right subject to the provisions of the preceding subsection would completely change its effect and as already stated would make it necessary for the secured creditor to obtain leave of the court before availing himself of his legal remedies in respect of the security. It will be readily appreciated that such a requirement would impose a considerable expense upon a bank which was seeking a speedy realization of its security and the delays which would almost certainly ensue in obtaining leave might result in serious depreciation of perishable goods upon which security had been given and consequent loss to the bank. The provision would be completely unworkable and would constitute an unjustifiable fettering of the rights of secured creditors.

PART IV

Administration of Assets

Section 39(11)—(13)—"Administrative officials, Superintendent may examine bank accounts . . . private records and documents, outside investigations"

These provisions do not expressly empower the superintendent to authorize accountants and others to act on his behalf in these examinations and investigations. The banks by reason of the banker-customer relationship are obliged to maintain secrecy concerning their customers' affairs and are liable for any unauthorized disclosure. It is necessary therefore that any legislative authorization to any government official to obtain information from the bank concerning a customer's affairs be clear cut and explicit and if any examination or investigation is to be conducted by anyone other than the superintendent he should be expressly empowered to authorize in writing such person to act on his behalf.

Section 68(1)—Avoidance of preference in certain cases.

The combined effect of this provision and of section 69(2), which thrusts the onus of proof on the person asserting the validity of the transaction, is that no transaction during three months prior to bankruptcy, within the meaning of the broad definition in section 2(*jj*), could stand unless the creditor could maintain the onus of proof thrust upon him by section 69(2). All creditors would have to proceed on the tenuous footing that every transaction was bad until proven to have been good.

The new test of voidability would be whether the transaction resulted in any person, creditor, etc., obtaining a preference, advantage or benefit over the

creditors or any one of them. It is proposed to discard the present basis where intent to prefer is the test, and all jurisprudence based thereon during the years since the statute was first enacted.

It will be recalled that in the Act of 1919, chapter 36, section 31(1), an alternative test of voidability was expressed in the words "or which has the effect of giving such creditor preference over the other creditors". In 1920, however, Parliament saw fit to transfer these words to the prima facie presumption provision in subsection 2 of the section. Such a presumption can be rebutted by evidence to the contrary.

In the proposed Bill the words "advantage or benefit" are added, making the test so broad that it would be difficult to imagine any transaction which would not result in one creditor obtaining some advantage or some benefit over the others or any one of them. As already stated in another connection, this could have serious results with respect to security validly given to a bank pursuant to the provisions of the Bank Act in consequence of a promise given by the creditor to the bank to give that security when required.

A decision under the present Act that the transfer by a bank of a credit from one account of a customer to an account in which there was a debit balance was not a conveyance, transfer or payment within the section might be held inapplicable under the proposed Act and might even be held to constitute a transaction which resulted in the bank obtaining a benefit over any one of the other creditors and be declared void. Such a decision might have a serious effect on ordinary banking procedure recognized by law under which a bank is entitled to consolidate its customer's accounts.

Under the present statute it has been held that payment of amounts due in the ordinary course of business would not be regarded as done with a view to prefer. The proposed revision would do away with that legislation and might be held to invalidate payments in the ordinary course by a customer to his bank of his obligations as they mature. It has also been held that a payment to a secured creditor was not within the provision but the new legislation might throw doubt upon the validity of such payments.

Section 68 (2)—Application of Provincial Enactments

It is probably not the intention that this provision would enable a trustee in bankruptcy, say in the Province of Quebec, to invoke any law of any other province in order to invalidate a transaction by a creditor in that province, yet the language is broad enough to permit the law of any other part of Canada to be invoked without regard to the locality of the debtor or of the property affected.

Some limitation should be added to the provision so the only provincial laws which could be invoked would be those of the province in which the bankruptcy took place, or in which assets of the bankrupt were situated at the time of the bankruptcy, or the province in which a transaction took place affecting property of the bankrupt.

A further question arises from this provision, namely whether it would have the effect of reviving certain provincial legislation relating to assignments and preferences which had been held valid prior to the enactment of bankruptcy legislation by Parliament but which since the passing of the Bankruptcy Act in 1919 has been deemed to be suspended.

Section 68 (3)—"secret transactions deemed unlawful"

It might be well to clarify the words "other person" in line 2 by the phrase "knowing him to be a bankrupt", in order to protect innocent transactions. In view also of the specific inclusion in section 68 (4) of the words "after the bankruptcy of any person", to have them inserted in line 1, subsection 3. Otherwise their omission from the one and inclusion in the other might give

rise to an interpretation that subsection 3 would cover any secret transaction prior to the bankruptcy. That might even be alleged to affect ordinary banking transactions between a bank and its customer as these are necessarily secret by implication of law.

Section 68 (5)—"admissibility of evidence of intent in disputed transactions"

This makes it clear that the effect of a transaction is to be the test regardless of intent. The proof of intent is still an essential factor under the criminal law. Should a man have the taint of fraud cast upon him if his intentions were honest? This proposed provision would constitute complete reversal of the present law and goes much further than seems necessary to resolve any confusion in existing decisions, a solution which might better be left to the mature consideration of the Supreme Court of Canada.

Section 69 (1)—"protected transactions"

It is submitted that this provision goes far beyond a simplified redraft of present section 65. The proviso to the present section 65 will protect certain transactions from avoidance if made (*a*) in good faith, (*b*) before the date of the receiving order or authorized assignment, and (*c*) without notice of any available act of bankruptcy. The proposed new provision would add the following requirements:—

(*d*) that the valuable consideration be adequate

(*e*) that there be no knowledge of the insolvency or commission of an act of bankruptcy

(*f*) that there be no reason to suspect insolvency or commission of an act of bankruptcy.

Moreover, the new provision may have left a gap between the filing of a petition of bankruptcy and the date of the receiving order or authorized assignment. Section 27 (4) of the Bill relates the bankruptcy back to the date of the filing of the petition. The new provision covers transactions before the bankruptcy and therefore could not save the validity of a transaction taking place between the filing of the petition and the date of the order.

Section 69(2)—"onus of proof"

The shifting of the onus in the manner proposed is so serious that it would be almost impossible to bring a transaction under the protection of the section. Every transaction would have to be carefully studied from the point of view of actual notice, available knowledge or reasons for suspicion, and unless a bank could be sure that it could positively establish that these were lacking and that good faith was therefore established, it could not afford to enter into the transaction.

In addition the question of adequacy of valuable consideration would arise, particularly with regard to security given either on goods or by way of additional or collateral security of any kind. It would be difficult to establish, for instance, that there was adequate consideration within the definition of section 2(*b*) for additional security given for a debt already incurred. In consequence a bank might refrain from taking additional security at a time when experience had indicated the desirability of such a course. It would follow that bank losses could be more serious than would otherwise be the case and the safety of the banking system would to some extent be jeopardized, all because the taking of additional security sanctioned by Parliament under the Bank Act for the purpose of protecting the depositors and the bank was made practically impossible by the provisions of bankruptcy legislation.

With all respect to the Superintendent of Bankruptcy, his knowledge and draftsmanship, it would seem that sections 68 and 69 should be replaced by the corresponding provisions of the present statute.

PART V

Creditors

Proof of Claims

Section 110(1)—"creditors shall prove claims"

The expression "as soon as may be" is rather indefinite, particularly as the new principle of the provision is that unless the creditor proves his debt "as soon as may be after the filing of the proposal . . . or after the bankruptcy he shall not be entitled to share in any distribution . . ." This is too drastic a penalty for a late filing, particularly when it is difficult to determine the last day for proof of debt. The expression "as soon as may be" is used in the present section 105(1) but it is not coupled with a penalty and the phrase does not seem to have received clear judicial definition.

Section 124—"mutual credits, debts or other dealings"

In the light of the expanded definition of "act of bankruptcy" in section 3 the last part of section 124 might interfere with a bank's exercise of its right of set-off.

Section 125(7)—"Trustee not liable for costs"

It is submitted that the question of liability for costs should be left entirely in the discretion of the court, particularly if the onus is shifted as proposed in section 69(2).

Section 126(1)—"priority of claims"

The subsection commences

> Subject to the rights of contractual secured creditors . . .

There need not be any reference to secured creditors, whether contractual or otherwise, because the section purports to deal only with the application of the proceeds realized from the property of a bankrupt, and has nothing to do with a creditor's security.

In any event, the word "contractual" should be deleted because it would not include

(*a*) any security the bank may have by way of banker's lien at common law, and

(*b*) a bank's statutory lien upon the shares of its shareholders for unpaid debts or liabilities under section 76 of the Bank Act.

Neither of these is contractual. There does not appear to be any need to mention secured creditors. The trustee is not dealing with their property. Their freedom of action to realize should, as hitherto, be unhampered. If the wording were changed to read "the proceeds realized *by the trustee* from the property of a bankrupt" there would be less objection to saying "subject to the rights of secured creditors" if the purpose is to accept such rights clearly from the provisions of section 126.

The foregoing suggestions are submitted, not in any spirit of adverse criticism, but with a keen appreciation of the difficulties encountered by the draftsmen of the Bill and in a genuine effort to present possible effects of the proposed Bill upon the banks, with some constructive proposals for overcoming the objections.

Respectfully submitted,

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Montreal, July 31, 1946.